

**ROHR ALERT!! Debt Relief**

1 message

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**Dear Subscribers,**

**We are of course not referring to any debt being forgiven, but rather the surprise turnaround in Republican Party resistance to providing Democrats any breathing room in fraught efforts to raise the US debt ceiling. Minority Leader McConnell came to Majority Leader Schumer Wednesday with the offer of a temporary debt ceiling hike, which would tide the government over until early December. Yet it is clear this 'olive branch' from McConnell was in no way any actual agreement with Democrats' aims, as noted in today's Reuters article (<https://reut.rs/3oHxW7I>.)**

**He is still insisting that they develop any major debt ceiling increase on their own, with Senate Republicans still filibustering any attempt to pass a hike on a simple majority vote. As noted in Wednesday's 'Risk-Off Trend Evolution' ALERT!! (repeated below for your ease of access), any requirement the Dems instead pass it through 'reconciliation' would cost them quite a bit more time and effort. That would effectively accomplish what many feel is McConnell's real purpose (see Wednesday's analysis) of distracting them from their goal of passing Biden's major 'social infrastructure' plan. That amounts to an immense dual burden.**

**And as far as the US equities have come back on the ostensible 'relief rally' with the December S&P 500 future back above the 4,348 area, it is also only up around the 4,410 significant weekly channel DOWN Break from two weeks ago (see the chart as of last Friday's Close <https://bit.ly/3FkeW58>.) That is also congestion from the August-September topping activity, reinforced by 4.427 weekly MA-13. This is therefore only a partial recovery from the previously noted 'Risk-Off Trend Evolution', pending whether it can indeed recover well above the low-4,400 area.**

**It is much the same for the foreign exchange loss of any 'risk-on' psychology. There is only a partial, selective recovery in emerging currencies, and the other developed currencies are still weak against the recently revived 'haven' bid in the US dollar. However, the improved psychology from any temporary US debt ceiling deal seems more the relief of an immediate stressor than any reason to look for a more upbeat overall psychology, as the 'macro' data still has some weak notes.**

**Both year-on-year German Industrial Production and Italian Retail Sales were much weaker than expected. And US Challenger Job Cuts were elevated again despite Wednesday's improvement in the ADP Employment Change. The latter bodes well for Friday's US Employment report, projected to gain nearly 500,000 jobs after a disappointing 235,000 gain in August. It's going to be interesting.**

**That is also because the global govies remain under pressure despite slightly weaker macro data. That is on an incipient 'stagflation' perspective, which allows for sustained high inflation despite any weakening of the global economy. It is therefore also possible that any strong US Employment report Friday might also be a classic case of 'good news is bad news'. After sagging below the low end of its 132-00/131-16 support into the middle of last week, the December T-note future bounced slightly above the top of it early this week. Yet despite the recent weak macro data, it is back to the low end at present. Any sustained weakness back below it late this week would indicate a resumption of the overall yield surge.**

December Gilt future continues to lead the way down on sustained UK inflation concerns, especially elevated energy prices. Having wiped out its mid-126.00 historic congestion last week, it did manage to rebound from the low 124.00 area this week. Any sustained weakness below that area points to interim congestion in the 123.00 and 122.00 areas, yet with the major low end of the full 2018 range (it is already sagging into) not until the 120.00 area (weekly MA-41 minus 9.00!!)

Yet the other issue we highlighted of late is the travails of the Chinese property market, both outright performance and its extremely fraught financial position. See previous analyses repeated below for more of our recent assessment along with links to external information sources citing the degree to which this problem goes well beyond the Evergrande debt and interest payment problem. On top of that there are potential extended effects back into the Chinese economy, which include classical dispersed sources of funding for the local governments as well.

This is highlighted in this morning's Reuters article (<https://reut.rs/3iGXFst>) on the knock-on effects of what are now weaker land sales. While there was always a sense that the Chinese property market would need to cool off at some point, the fact the central government is leaning into it at present makes this the inflection point where lower expectations are now ingrained into the market. And that is likely to hurt funding for local governments which are dependent on those sales.

This central government mucking with the real estate market is reminiscent of US government tax reform in the mid-1980s: the Tax Reform Act of 1986 ('TRA86'). This was not necessarily an overall negative act in its own right, as it lowered the top marginal tax rate from 50% to 28% (see the WIKI <https://bit.ly/3oH4qjc>.)

Yet note the section slightly below the halfway down in that WIKI on 'Passive losses and tax shelters'. As the article notes, "*This contributed to the end of the real estate boom of the early-to-mid 1980s, which in turn was the primary cause of the U.S. savings and loan crisis.*" Not noted in the article is this was applied retroactively (!!) to all passive investment; This meant elimination of deductions from previous investments, leading to a dearth of real estate investment.

That in turn led to major property price declines from what had previously been unrealistically elevated levels. Across time the weight on the economy from the extended effects (weaker construction and local business receipts, less general investor spending, etc.) of weakness in this important sector translated into the long 1989-1991 US recession (see the St. Louis Fed graph <https://bit.ly/3oCiyJH>.)

That took some time to develop, as the full impact of 'TRA86' was not necessarily immediately clear, due to many developers, real estate syndication firms offering 'tax advantaged' investments and investors trying to minimize the net effect. Yet it is that much more apparent in the Chinese property market due to the high profile offshore borrowing by the sector. Might this be mitigated by some sort of central government bailout? Possibly. Yet that would fly in the face of President Xi's current drive to equalize what has been lopsided wealth accumulation into the next major Chinese Communist Party Congress just one year from now.

That is compounded by the degree to which so much of the Chinese middle class has quite a bit of its wealth, and some degree of its current well-paid employment, tied into the Chinese property market and its developers. That said, any bailout which seems to rescue the wealthy senior managements of these companies is not likely an acceptable alternative, leaving quite a bit of risk in their economy.

Yet in the wake of the temporary US debt ceiling deal, removal of that near-term stressor leaves the immediate fate of markets with how they respond to Friday's US Employment report (and to a lesser degree its Canadian counterpart.) In case the numbers are as strong as the ADP Employment Change and US Weekly Initial Jobless Benefits Claims indicate, we suggest close observation of the global govvies for any sign of a '*good news is bad news*' psychology taking hold.

Courtesy Repeat of Wednesday's 'Risk-Off Trend Evolution' ALERT!!

Sometimes we revert to our concept that in the opinion sweepstakes the markets get the final say. And of late the price activity has reversed from the previous 'risk-on' psychology into a 'risk-off'

tendency across the board. That means not just US equities, but both the developed currencies and emerging currencies, with the inflation driven weakness of the global govvnies adding to the mix.

That inflation factor being linked to the supply bottlenecks even most sanguine central bankers now allow will last longer than previously hoped is an ongoing negative factor. Yet the degree to which it might be in the context of a weakening global economy as well makes it the first bona fide ‘stagflation’ potential since the 1970s (as previously reviewed.) The risk of a slower economy is focused on the possibility the US fiscal stimulus in the form of infrastructure spending might be further delayed, and the potential for Chinese property problems to balloon.

On the former, there is a natural drag from the now very prominent disagreement between Democratic Party moderates wanting immediate passage of bipartisan ‘classical infrastructure’ legislation versus progressives who want that to only succeed if their more expansive ‘social infrastructure’ plan is passed. And even that contentious intraparty divide is exacerbated by the debt ceiling problem.

Democratic Senator Chris Coons was interviewed on CNBC this morning, and was whining about the Republicans invoking the filibuster to block Dems from readily passing a debt ceiling hike on a simple majority vote. And Republican Senate Minority Leader Mitch McConnell repeatedly saying the Democrats can easily pass the debt ceiling hike is a bit specious. He knows Coons’ complaint that using ‘reconciliation’ to pass it by a simple majority is a far more laborious and time consuming process is true, and will need to be done by next Thursday.

Then the real truth (yes, every once in a while it slips out even in Washington DC) came from Coons: (paraphrased) *“McConnell’s real purpose in forcing us to use time consuming and labor intensive reconciliation is to distract us from working on President Biden’s more major \$3.5 trillion ‘social infrastructure’ legislation.”* Which is to say spend more time in the fraught negotiations between Democratic moderates and progressives currently at loggerheads on the individual program specifics and total funding. Gee, a minority party using all tools at its disposal to hamper the agenda of the majority? STOP THE PRESSES for this breaking news!!

Or not. This is not just the tactics seen many times before in the US... It is a universal political axiom, and it is surprising to hear Coons gripe about the time it is going to take. That is amplified by the fact that McConnell had signaled the Democrats almost three months ago that he would insist the Democrats pass the debt ceiling hike on their own as long as they were going to pursue the far more major ‘social infrastructure’ spending. His position is that the Democrats would already be well along in the reconciliation process if they had started back then.

The bad news for Democrats is that they are going to need to take time away from those very fraught negotiations between their moderates and progressives on finally passing the bipartisan \$1.2 trillion classic infrastructure deal, which will require a meeting of the minds on far more expansive ‘social infrastructure’.

That is with a self-imposed end of October deadline (pushed from September 27th) for the vote on the ‘classical infrastructure’ bill looming large. It is looking much more challenging in the context of critical debt ceiling reconciliation talks... Trick or Treat! It is still likely some sort of infrastructure deal will be cobbled together by Democrats, as going back to their constituents with nothing to show for the first year of a Presidential administration would create more weakness into the already challenging 2022 midterm elections where they are vulnerable.

Yet the longer it is delayed, the more so it looks like the Democratic majority (even allowing how slim it may be) is having trouble governing. Along with the various hits to President Biden’s poll rankings on quite a few fronts, that is a real risk for them. The delay also means any government largesse flowing to their constituents is already significantly delayed, with less positive impact.

Then there is the Chinese property market and finance situation. As we have already reviewed in some depth in Tuesday’s ‘The Clock is Ticking’ ALERT!! (repeated below for your ease of access.) And we still recommend a read of that analysis, and especially linking into the Reuters article that has so much more information on the broader aspects of the Chinese property market problems.

There is review of at least several other companies' problems outside of the obvious Evergrande missed interest payment issues... as it turns out they are not alone in recent ir anticipated international debt interest payments. Once again, while this is not likely to turn into an international financial crisis (too little exposure among Western banks and investors), any significant weakening of the Chinese economy will still be an issue for the rest of the world.

Regarding the market getting the final say on the trend evolution, the US equities reaction from the early September front month S&P 500 future 4,549.50 last new all-time has lasted over a month. That is compared to previous 'quick hiccups' in May, June, July and August that were basically all in one week, with subsequent recovery to and through the previous all-time highs not too long after that.

This is the tendency as well for developed currencies and emerging currencies, which (outside of the Crude Oil-advantaged Russian ruble) have been under sustained pressure for approximately the same length of time. And in each case the inability to recover back above previously violated support is an earmark of a more sustained near-term bear trend. Does that equate to a major trend reversal?

That cannot be known until the markets reach lower, more major supports. Yet it is the case that those lower levels are more likely to be seen under the auspices of the degraded 'macro' influences noted above along with other influences. Using the US equities as a benchmark for when the trend becomes more critical for the overall 'risk appetite', we suggest the December S&P 500 future failing into no better than roughly the violated 4,348 support could easily see the lower 4,235-00 range or even the low 4,100 area. That would equate to further weakness in the non-US dollar foreign exchange, and potentially be exacerbated by any further weakness in the global govies on inflation indications remaining bad.

Courtesy Repeat of Tuesday's 'The Clock is Ticking' ALERT!!

The typically multiple macro factors necessary to weigh on the US equities were extensively reviewed in Monday's 'Shifting Macro' ALERT!! (repeated below for your ease of access.) Those are primarily concerns over the weakening of the Chinese economy that is spilling over more broadly into Asian economic issues, at this point also meaning international trade concerns on product availability and supply lines into other economies. We revisit another aspect of that below.

We also reviewed the US fiscal picture as it regards the current stall and potential overall failure of the Biden administration's bipartisan \$1.2 trillion infrastructure plan due to the Congressional impasse with Democratic Party progressives demanding the concurrent passage of the \$3.5 trillion 'social infrastructure' plan. The need to delay the vote on the \$1.2 trillion infrastructure plan until the end of this month is a risk. That is regardless of how much anyone would like to believe the Democrats failing to pass that is tantamount to 'political suicide' (as we suggested in Friday's 'Charge of the Flight Brigade' ALERT!! (also repeated again below for your ease of access.) Yet there is a much more critical horizon...

...in the form of the need to raise the US government debt ceiling, the failure of which will leave it unable to pay its bills after the October 18th deadline. It is the classical 'received wisdom' that this has come close before, and "*they'll never let that happen.*" However, there are contingencies discussed in Monday's Reuters article (<https://reut.rs/2YvPIFs>) around whether Republicans longstanding signal that they will not vote for the debt ceiling increase is a real stumbling block.

Or is it more so as Senate Minority Leader McConnell holds, that Democrats are averse to raising the debt ceiling on their own through 'reconciliation' (needing only the 50 Senate votes the Democrats control) due to not wanting to appear solely responsible for raising it. That could be used against them in political campaigns, which is also the height of hypocrisy by the Republicans. During the Trump administration the Republicans raised the debt ceiling three times (with the cooperation of the Democrats) increasing the national debt by \$8 trillion.

Yet it is a bit more complex to implement reconciliation, and will distract the Democrats from addressing their internal dueling infrastructure plan resolution. As troubling as the potential US payment default and cancellation of many internal payments to Social Security and Veterans Benefits

recipients may be, it is likely to be resolved. The Democrats cannot possibly allow it to fail by next Thursday's deadline without invoking another form of political suicide.

However, the other main issue for US equities and overall risk appetite, thereby affecting the global govies and foreign exchange as well, is Chinese economic fortunes intensified by the problems in their property sector. Another Reuters article (<https://reut.rs/3izTaAh>) this morning highlighted how Evergrande's cash flow and debt payment problems were likely spilling over (at least mildly for now) into other Chinese property companies. The good news is that Evergrande's sale of some assets has provided it with \$5 billion. While that may address its need to make deferred interest payments later this month, it remains an issue.

That amount only covers a sliver of Evergrande's \$300 billion of debt. It will be interesting to see what transpires when the 'grace period' for its September 23rd missed interest payment lapses on Saturday, October 23rd. On current form, it will likely have the funds to make that payment and address other near-term payments due later this year. However, as the article notes, any discounted 'fire sale' prices for Evergrande assets will affect other Chinese property companies.

And Evergrande debts are only part of the problem, as it is also on the hook to still develop 1.6 million homes for which it has taken deposits along with forced investments made by many employees (a condition of continued employment) to the tune of \$145 million, characterized as high interest loans. It was the case that the employees were threatened with the loss of performance pay and bonuses.

However, the company recently stopped repaying those loans even prior to missing its dollar-bond payments over the past two weeks. It employs over 120,000 people in many Chinese cities, where the local economies also rely on commerce from those folks. Sounds a lot like the US situation back in 2008, which was also a slow motion train wreck due to near-term stop-gap measures.

Some of the scariest bits of information over the past several days have been the citations by various financial 'experts' that Evergrande is only a small part of the Chinese debt market, and cannot possibly cause a more general meltdown in such a major Chinese economic sector, which commands 40% of national wealth. However, this is reminiscent of the folks (including Fed Chair Bernanke at the time) who cited subprime mortgages as only comprising a small percentage of the overall US housing finance market. Look at how well that turned out.

The blessing at this point is that the broader global financial industry and general investment community are not significantly exposed. That is due to the previous Chinese restrictions on 'foreign' investment in so many of its industries. While it might have seemed a bit xenophobic at the time, Mr. Xi and his minions appear to have done the rest of the world a favor. Yet to be clear, any major weakening of the Chinese economy will still represent a sustained drag on the global economy.

Courtesy Repeat of Monday's critical consideration

After the early July downside reaction the recovery back above the 4,300 area violated support left the higher resistance into the previous week's 4,360 DOWN Closing Price Reversal with a Tolerance to 4,364. That is clear on the S&P 500 future weekly chart (<https://bit.ly/3FkeW58> updated through Friday.) It is of note the September S&P 500 future had managed to retest that area right into the ECB press conference prior to weakening once again the following Thursday morning.

And the September S&P 500 future subsequently sustaining activity above the 4,425 and 4,450 weekly Oscillator thresholds was a sign of continued strength as they were still rising \$25 per week. As such, the Oscillator indications remained important after what was the 'lackluster jailbreak' after the previous outstanding US Employment report. With the market dropping back below the 4,450 level (on weekly MA-41 up \$25), there seemed to finally be some real risk.

Yet even below the key lower interim levels into the recent 4,425 area congestion and 4,380-65 area bottom of that, it also held key lower support in mid-August looking forward into the following week. That bigger level was 4,340 on weekly MA-13 (loosely held on all sharp reactions) at that time, and the significant aggressive weekly UP Channel from the major 2,174 March 2020 cycle low.



In the event, the recent late week recovery back above the 4,425 area pointed to the strength of the psychological recovery as well as exceeding the key technical resistance areas. That led to the recent new all-time highs above the previous week's 4,476.50 trading high (prior to the temporary selloff.) That again left the near-term Oscillator thresholds into 4,515 and 4,540 areas (on the rising MA-41), which it failed to maintain in early September, fomenting the reaction.

This led to the violation of the 4,492 interim daily chart congestion after trading around it previous, with the more prominent 4,462 area also being violated two weeks ago. And while it traded back above that as well early last week, recent softening below it spoke of an ability to trend lower in the near term. That left the more major 4,420-10 area as next support on both weekly MA-13 as well as that significant aggressive weekly UP Channel from the major March 2020 low.

Having tested that area into the Close three weeks ago and violating it from the beginning of last week was a fresh 4,410 DOWN Break. That fed further weakness which was already anticipated from the negative fundamental influence flowing out of China. As usual there is a Tolerance below that (as seen on selloffs in both June and July) down to the 4,350 area lower congestion developed during the temporary July topping activity, and retested on the mid-August sharp temporary reaction to a 4,347.75 trading low. While that may seem to be a broad berth, on past form only below the 4,350 area does the market signal a full trend reversal.

Yet as always with these matters, the weekly Close was more important than temporary trading weakness below it. And the December S&P 500 future held overall against interim low-4,300 support, and ended the week back above the low 4,400 area. The extent of the temporary selloff means that it needed to be treated as a 4,410 weekly up channel DOWN Break. Yet that also means the Close back above it established it as a Negated DOWN Break, and therefore a support area. That is also consistent with weekly MA-13 moving up to the 4,430 area this week.

That said, the 4,348 area had reverted to the key support again last week on renewed pressure. And much like previous, it was temporarily violated early last week. The difference is that the daily 'trend flow' is a bit different, where the previous week it was seriously violated on Monday and churned around it on Tuesday prior to recovering so well. Last week it slipped on Tuesday, and was churning around it early Thursday with much less slippage.

Yet it ultimately failed even worse than the previous week, and the late week Merck news only left it retesting that failed 4,348 support. The lower supports are into the 4,235-00 range May-June congestion it surmounted in late June. If that should fail to hold, there is also prominent congestion back into the low-4,100 area, with weekly MA-41 in the mid-4,100 area along the way.

Thanks for your interest.

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